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IN THE

Supreme Court of the United States

OCTOBER TERM, 1961.

HOUSEHOLD FINANCE CORPORATION,
Appellant,

vs.

DIRECTOR OF THE DIVISION OF TAXATION, DEPARTMENT OF THE TREASURY OF THE STATE OF NEW JERSEY,
Respondent.

ON APPEAL FROM THE SUPREME COURT OF NEW JERSEY.

JURISDICTIONAL STATEMENT.

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July 9, 1962.

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Respondent.

ON APPEAL FROM THE SUPREME COURT OF NEW JERSEY.

JURISDICTIONAL STATEMENT.

Appellant appeals from the judgment of the Supreme Court of New Jersey entered January 22, 1962 (rehearing denied March 26, 1962) affirming the judgment of the Division of Tax Appeals, Department of the Treasury of the State of New Jersey, entered March 6, 1961. The Supreme Court of New Jersey is the highest state court available to appellant. New Jersey Constitution, Article VI, Section II, Paragraph 2.

Opinions Below.

The opinion of the Supreme Court of New Jersey, dated January 22, 1962, is reported at 36 N. J. 353, 177 A. 2d 738. A copy of the opinion, order on petition for rehearing and mandate are attached hereto as Appendix A, pp. 1a-15a. The opinion and judgment of the Division of Tax Appeals (unreported) are attached as Appendix B, pp. 16a-35a.

Jurisdiction.

Appellant, a Delaware corporation, and its subsidiaries in the aggregate conduct a financial business in most of the United States and Canada.

This is an appeal from a judgment affirming a franchise tax imposed under a New Jersey statute which denied due process and the equal protection of the law in that as imposed it resulted in the taxation of corporate extraterritorial value. Under the statute the net worth of appellant, a multistate corporation, was allocated for franchise tax purposes under a gross receipts fraction, in which the gross receipts in the numerator and the gross receipts in the denominator, respectively, had no comparable relation to net worth.

This action was brought under the provisions of the New Jersey Financial Business Tax Act (N. J. S. A. 54:10B-1 *et seq.*) to obtain a reversal of the redetermination of the Director of the Division of Taxation, Department of the Treasury of the State of New Jersey of appellant's tax liability for the four tax years 1954 through 1957. The judgment of the Supreme Court of New Jersey is dated January 22, 1962, was entered on said date, rehearing was denied on March 26, 1962, and notice of appeal to this Court was filed in the New Jersey Supreme Court on May 11, 1962.

Jurisdiction of this appeal is conferred on this Court by 28 U. S. C. §1257(a), 62 Stat. 929, and such jurisdiction is confirmed by *Railway Express Agency* v. *Virginia*, 358 U. S. 434, 79 S. Ct. 411, 3 L. Ed. 2d 450 (1959); *Butler Bros.* v. *McColgan*, 315 U. S. 501, 62 S. Ct. 701, 86 L. Ed. 991 (1942); *Connecticut General Life Ins. Co.* v. *Johnson*, 303 U. S. 77, 58 S. Ct. 436, 82 L. Ed. 673 (1938); and *Hans Rees' Sons, Inc.* v. *North Carolina*, 283 U. S. 123, 51 S. Ct. 385, 75 L. Ed. 879 (1931). Jurisdiction by writ of certiorari exists

under 28 U. S. C. §1257(3), 62 Stat. 929; 28 U. S. C. §2103, 62 Stat. 962 and the authority of *Charleston Federal Savings and Loan Association* v. *Alderson*, 324 U. S. 182, 65 S. Ct. 624, 89 L. Ed. 857 (1945), rehearing denied 324 U. S. 888, 65 S. Ct. 863, 89 L. Ed. 1436 (1945).

Statutes and Constitutional Provisions Involved.

The pertinent provisions of New Jersey Financial Business Tax Act (N. J. S. A. 54:10B-1 *et seq.*), the validity of which is involved, are attached as Appendix C pp. 36a-41a.

In summary, the act imposes an annual franchise tax measured by the taxpayer's "net worth". N. J. S. A. 54:10B-3. Net worth is defined as the aggregate of capital stock, capital and earned surpluses, surplus reserves and indebtedness owing by the taxpayer to substantial stockholders, N. J. S. A. 54:10B-2(c)(1). Where the taxpayer does business in more than one state, the act provides for apportionment of total net worth so as to determine "the value of its net worth * * * within this State", this apportioned net worth becoming the taxable net worth. The apportioned net worth is the same proportion of total net worth as the proportion of local gross receipts to total gross receipts. N. J. S. A. 54:10B-8. Gross receipts are defined as the aggregate of compensation for financial services, gross profits from trading in securities, interest and dividends received on securities, interest charged to customers on margin accounts and other gross income resulting from the operation of a financial business. N. J. S. A. 54:10B-8. The amount of the tax is determined by multiplying the net worth apportioned to New Jersey by the tax rate of 0.75%. N. J. S. A. 54:10B-3.

The provisions of the United States Constitution involved herein are the due process and equal protection

clauses of the Fourteenth Amendment, Section 1 (hereinafter referred to as "the 14th Amendment").

Questions Presented.

1. In allocating appellant's net worth for state franchise tax purposes by a gross receipts fraction where the fraction's numerator reflecting *local* business is appellant's gross receipts from its customers within the taxing state, and where its *total* business (including that located out of the taxing state) is reflected by a denominator composed of gross receipts of an entirely different type in large part having a substantially lower relation to net worth, does such lack of comparability as between the numerator and the denominator violate the 14th Amendment because it results in taxing extraterritorial values?

2. In allocating appellant's net worth, including a substantial amount of out-of-state assets which are necessary to its business but which directly produce no gross receipts, does the use of a gross receipts allocation fraction violate the 14th Amendment because it results in taxing extraterritorial values?

Statement of the Case.

The issue is whether a method for apportioning appellant's net worth within and without New Jersey violates the Fourteenth Amendment. Appellant is an international as well as an interstate corporate organization with all of its headquarters outside New Jersey. Its net worth is allocated under the New Jersey Financial Business Tax Act for the purpose of assessing a franchise tax on the basis of a gross receipts fraction. As applied to

appellant's facts the gross receipts in the numerator and in the denominator of the allocating fraction had no comparable relation to net worth. This resulted in the allocation of extraterritorial values to New Jersey for franchise tax purposes in violation of the Fourteenth Amendment.

The New Jersey Financial Business Tax Act imposes an annual franchise tax on the taxpayer's net worth. Net worth is defined as the aggregate of capital stock, capital and earned surpluses, surplus reserves and indebtedness of a taxpayer to substantial stockholders. Where the taxpayer does business in more than one state, the act provides that its net worth shall be allocated within and without the state, according to the proportion of its local gross receipts within the state to its total gross receipts during the tax year.

All of appellant's equity investment in and advances to its Canadian subsidiaries and in and to its United States subsidiaries were included in computing appellant's net worth.* But instead of adding the gross receipts from these subsidiaries' customers to appellant's gross receipts in the allocation denominator supposedly reflecting appellant's entire business, the respondent Director added:

> with respect to its Canadian subsidiaries—a substantially smaller figure made up of interest, dividends, and the supervision fees paid by these Canadian subsidiaries to appellant, and
>
> with respect to its United States subsidiaries—a substantially smaller figure made up of interest and the supervision fees paid by them to appellant. No dividends were received by appellant on its stock in its United States subsidiaries, with a minor exception of a small liquidating dividend received in 1950.

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*None of appellant's liabilities, against which its assets were netted, were earmarked or specially allocable to any particular asset or class of assets.

Appellant's net worth also included net values for approximately $21,000,000 to $24,000,000 of other assets necessary to the operation of its business from which appellant directly derived virtually no gross receipts.

All of appellant's investment in and advances to its subsidiaries and in the approximately $21,000,000 to $24,000,000 of other assets had a tax situs outside New Jersey.

By this method, the gross receipts total in the denominator of the allocating fraction is lower in relation to net worth than is the gross receipts total in the numerator. As a result the two factors had no comparable significance as a means of valuing net worth. As applied to appellant's facts this statutory formula allocated extraterritorial value to New Jersey.

It was appellant's contention below and here that if in the application of the statute the taxpayer's total receipts are understated, or the taxpayer's New Jersey receipts are relatively overstated, extraterritorial values are taxed in New Jersey in violation of the 14th Amendment.

As developed from the evidence, the violation of the 14th Amendment is demonstrated by the following comparative figures:

	1954	1955	1956	1957	Total
Total consolidated net worth	$124,731,816.00	$133,803,622.00	$147,068,244.00	$164,312,548.00	—
New Jersey gross receipts	3,340,969.00	3,422,355.00	3,290,420.00	3,398,595.00	—
Total gross receipts per Director	59,461,784.00	72,490,620.00	75,071,317.00	93,971,384.00	—
Actual consolidated gross receipts	82,662,817.00	89,492,255.00	97,185,019.00	114,965,950.00	—
New Jersey taxable % per Director	5.6187	4.7211	4.3831	3.6166	—
New Jersey taxable % based on actual consolidated gross receipts*	4.05	3.82	3.37	2.95	—
Taxable net worth per Director	7,008,307.00	6,317,003.00	6,446,148.00	5,942,526.00	—
Taxable net worth using consolidated gross receipts for apportionment ratio	5,051,639.00	5,111,298.00	4,956,200.00	4,847,220.00	—
Tax per Director	52,562.30	47,377.52	48,346.11	44,568.96	$192,854.89
Tax using consolidated gross receipts for apportionment ratio	37,887.29	38,334.74	37,171.50	36,354.15	149,747.68
Excess tax on extraterritorial value**	14,675.01	9,042.78	11,174.61	8,214.81	43,107.21

* Appellant does not advocate a consolidated gross receipts allocation formula or an allocation formula based on any other specific theory. That is the State's responsibility. The above figures merely demonstrate that when a State requires the use of gross receipts from customers as the numerator of an allocation fraction, the use of a different type of gross receipts in the denominator which are not comparable and bear a lower ratio to net worth arbitrarily allocates extraterritorial values to the taxing State.

** These data disregard a relatively very minor addition made by the respondent Director to appellant's taxable net worth and tax by virtue of certain uncontested adjustments made by him in total gross assets. For example in 1955 only about $140,000 was added to the tax base by uncontested adjustments, resulting in an uncontested tax increase of only about $1,050. Also disregarded as irrelevant and *de minimis* is a liquidating dividend received by appellant in 1956 from one of its United States subsidiaries.

The foregoing comparative figures demonstrate that the New Jersey tax penalizes the use of corporate subsidiaries and disregards headquarters values located outside New Jersey. The New Jersey Supreme Court confirmed this in stating:

> "There is nothing inherently wrong with the statutory plan. The alleged hardship ensued solely from Household's decision to operate in part through subsidiaries." Appendix A, p. 9a.

The Court also stated:

> "• • • [T]he location of headquarters was of no moment. • • • [T]he tangible property stationary at Chicago was devoted to New Jersey activities with the same immediate effect as if the equipment were within our borders." Appendix A, p. 6a.

The unconstitutional application of the New Jersey formula under the 14th Amendment was first raised in the proceedings instituted by appellant in the Division of Tax Appeals, Department of the Treasury of the State of New Jersey, the primary forum for tax appeals of this type in that state (see Appendix E, pp. 45a-47a); and was passed upon by the Supreme Court of New Jersey after that Court certified the proceedings directly to it on appeal from the Division's judgment to the Appellate Division of the Superior Court of New Jersey, (see Appendix A, pp. 5a, 7a, 8a, 10a-11a, 13a; Appendix D, pp. 42a-44a). The Supreme Court of New Jersey, after specifically dealing with the constitutional issues discussed herein, decided them adversely to appellant. See Appendix A, id.

THE QUESTIONS PRESENTED ARE SUBSTANTIAL AND OF GREAT PUBLIC IMPORTANCE.

INTRODUCTION.

Appellant respectfully argues that clear and cogent evidence was presented in these proceedings of the extraterritorial impact upon appellant of the New Jersey franchise tax for each of the four years in issue. By uncontradicted and comprehensive accounting and financial data and expert opinion evidence, appellant proved not only the extraterritoriality of the values so taxed, but the value thereof and the reasons why the tax had such effect.

By the application of the tax New Jersey has deprived appellant of its property without due process of law and has deprived it of the equal protection of the laws. In so doing, the State has disobeyed the constitutional principles of state franchise taxation of a multi-state foreign corporation enunciated in *Wallace* v. *Hines*, 253 U. S. 66, 64 L. ed. 782, 40 S. Ct. 435 (1920); *Hans Rees' Sons* v. *North Carolina, supra; Butler Bros.* v. *McColgan, supra;* and other decisions of this Court. Appellant contends that the statutory fraction was unsuitable in fact and in economic theory for the allocation of a total net worth which included substantial values reflecting headquarters assets and functions and subsidiary investment. Appellant showed: (1) that the statutory fraction inherently and necessarily mismeasures the portion of any taxpayer's net worth reflecting non-revenue-producing headquarters; and (2) that the fraction, being applied upon the basis of intercompany receipts by appellant from its subs instead of the gross receipts of the subs themselves, in fact mismeasures the portion of net worth reflecting the full net value of appellant's investment in wholly-owned subs which themselves received gross receipts. At each point

of mismeasurement the fraction introduced into the New Jersey tax base values which were concededly extraterritorial, and which should therefore be immune to taxation under the 14th Amendment.

I.

The evidence proved taxation of extraterritorial values.

In lieu of reviewing in detail appellant's evidence in this jurisdictional statement, its ultimate thrust can be summarized by three simple examples illustrating how the New Jersey tax statute as applied penalizes the use outside New Jersey of subsidiaries and non-revenue-producing headquarters values.

If appellant had had only one branch office which was in New Jersey and only one subsidiary which was in Canada, each representing a one million dollar investment; and if the branch office and the subsidiary each did a gross business of $100,000 and the subsidiary expended or retained all of its gross receipts, making no payment to appellant, the entire two million dollar net worth of appellant would be allocated to and taxable by New Jersey.

The same result would be reached if appellant owned ten million dollars in cash or other non-revenue-producing net assets with a tax situs outside New Jersey, and had a one million dollar investment in a single branch office operating in New Jersey. Under the theory of the New Jersey Supreme Court, the entire eleven million dollar net worth of appellant would be subject to taxation by New Jersey.

As to the use of corporate subsidiaries, the New Jersey Supreme Court says below:

> "We are not told why Household employed subsidiaries. *A probable motivation was tax advantage somewhere.* The question is whether a state must

adjust its tax laws to avoid a disadvantage a taxpayer may experience because of its decision to incorporate a part of its operation." (Emphasis added) Appendix A, p. 10a.

The purpose served by the use of the subsidiaries is not relevant to the issue of whether the New Jersey allocation fraction allocates extraterritorial values to New Jersey in violation of due process and equal protection. However, in view of the Court's statement, it is pertinent to point out that in appellant's multistate operation, it is necessary to take into account the laws of *all* of the states, the Dominion of Canada, and its provinces where those subsidiaries operate. For example, it is not unreasonable that all Canadian operations should be by Canadian subsidiaries exclusively subject to the laws of that country.

The mere fact that taxpayer has decided

"to incorporate a part of its operation"

does not remove it from the protection of the due process and equal protection clauses, as the New Jersey Supreme Court seems to suggest.

The New Jersey Supreme Court also said:

"• • • the Director, in preparing the allocation fraction, did not include the gross receipts of the subsidiaries, but rather only such sums as Household received from them • • •.

• • • • • •

The sums so paid to Household were less than the gross receipts of the subsidiaries." Appendix A, pp. 9a, 4a.

This use of income from appellant's subsidiaries which the Court stated was

"less than the gross receipts of the subsidiaries"

does not value the portion of net worth attributable to its investment in the subsidiaries by a method comparable to that used to value the portion of net worth attributable to its directly owned New Jersey branch offices.*

The headquarters offices of appellant are located in states outside the State of New Jersey and are, therefore, subject to franchise and property taxation by each of the states wherein they are located. Nevertheless, the Court below stated:

> "Hence in assaying the value of the business privilege in this State, the important thing is the business done here. In this frame of reference, the

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* Appellant's expert witness testified that the use of income from subsidiaries

> "is not a valid method of apportionment. It creates a great distortion, because, while it is based on gross receipts, the gross receipts of the different components of the business are *not the same types of gross receipts*, * * * And, to elaborate on those gross receipts, the gross receipts of the component of the business, that is branches outside of New Jersey and also that of the branches in New Jersey, is the money that the branches have taken in from customers to whom they have lent money.
>
> "The gross receipts of Household Finance Corporation, the taxpayer, from the component of its business, that is investment in subsidiaries, is simply whatever dividends they may happen to pay to the parent company and whatever interest they pay on money borrowed from the parent company.
>
> "Looking beyond the parent company to the gross receipts of the subsidiaries' portion of the business that would be comparable to the gross receipts of the branch business in New Jersey and outside of New Jersey, it would be the actual gross receipts that those subsidiaries received from their customers, rather than simply the interest and dividends from the subs.
>
> "There are two defects in interest and dividends, one being they are in effect something less than the net profit of the subs, the other being that they can vary from year to year, according to how the subs happen to pay them to the parent, without regard to the actual net worth in that investment in subs during that year."

Upon cross-examination, the State's own witness conceded that the Director's method was applied in literal compliance with the statute and without reference to equity, justice or business reality, and he also conceded that various other methods of allocation suggested by Taxpayer were theoretically sound.

> location of headquarters was of no moment. * * * the tangible property stationary at Chicago was devoted to New Jersey activities with the same immediate effect as if the equipment were within our borders. * * * the headquarters assets were wholly unproductive within the walls of the home office; * * *." Appendix A, p. 6a.

Thus, the valuation of the portion of net worth attributable to appellant's headquarters outside New Jersey based upon assets ranging from $21,000,000 to $24,000,000 but which were

> "* * * wholly unproductive within the walls of the home office"

by the gross receipts method is not comparable to valuing the portion of net worth attributable to taxpayer's New Jersey branch office assets yielding approximately 24% in gross receipts before costs. Similarly, if appellant moved its $24,000,000 of headquarters gross assets into New Jersey for the purposes of holding, protecting and using them there, by its headquarters staff of 431 persons, this obvious expansion of its local franchise would be virtually tax-exempt.*

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* This is an example of the temptation of a state to use its tax laws not for revenue but for promotion of local industry. The New York State Tax Structure Committee Interim Report of June 22, 1960, pp. 79-81, describes the results of sales-to-destination allocation as follows:

> "In general the tax will be reduced on firms selling elsewhere goods manufactured in New York state, and will be increased on firms selling in New York goods manufactured in other states. . . . The annual revenue loss of this revision in the sales factor may be expected to be about eight million dollars."

Foreign firms, however, have few if any "political restraints" which they can exert upon the taxing state. *McGoldrick* v. *Berwind-White Coal Mining Co.*, 309 U. S. 33, 44, 84 L. ed. 565, 570, 60 S. Ct. 388 (1940).

II.

The Fourteenth Amendment forbids the taxation of extraterritorial values.

Fortunately this case does not involve the Commerce Clause. The issues arise solely under the 14th Amendment. Under that Amendment the basic applicable law is simple, well-settled, and unchallenged. The controlling cases are *Hans Rees' Sons, Inc.* v. *North Carolina, supra,* and *Wallace* v. *Hines, supra.*

The famous case of *Butler Bros.* v. *McColgan, supra,* expressly recognized that the validity of an apportionment formula may be challenged by

> "clear and cogent evidence that it results in extraterritorial values being taxed."

This language from *Butler Bros.* was quoted by the Court with approval as late as 1959 in *Railway Express Agency* v. *Virginia, supra.*

The principle was stated in *Alpha Portland Cement Co.* v. *Massachusetts* (1925) 268 U. S. 203, 69 L. ed. 916, 45 S. Ct. 477, in terms of "property" instead of "values" as follows:

> "It must be regarded now as settled that a state may not . . . tax property beyond her borders . . . [T]he 14th Amendment does not permit taxation of property beyond the state's jurisdiction . . .
>
> • • • • • •
>
> "The local business of a foreign corporation may support an excise measured in any reasonable way if neither interstate commerce nor property beyond the state is taxed."

The same principle was expressed in terms of corporate franchises in *Great Atlantic & Pacific Tea Company* v. *Grosjean,* (1937) 301 U. S. 412, 81 L. ed. 1193, 57 S. Ct. 772, as follows:

> "The state may not tax real property or tangible personal property lying outside her borders; nor may she lay an excise or privilege tax upon the exercise or enjoyment of a right or privilege in another state derived from the laws of that state and therein exercised and enjoyed."

The same principle was expressed in terms of "profits" in the famous case of *Hans Rees' Sons* v. *North Carolina* (1931) *supra* as follows:

> "When, as in this case, there are different taxing jurisdictions, each competent to lay a tax with respect to what lies within, and is done within, its own border, and the question is necessarily one of apportionment, evidence may always be received which tends to show that a state has applied a method which, albeit fair on its face, operates so as to reach profits which are in no sense attributable to transactions within its jurisdiction."

The same principle indeed is inherent in every decision in which the validity of an apportionment formula under the 14th Amendment has been considered by the Court, for, as the Court said in *Wallace* v. *Hines, supra:*

> "The only reason for allowing a state to look beyond its borders when it taxes the property of foreign corporations is that it may get the true value of the things within it, when they are part of an organic system of wide extent, that gives them a value above what they otherwise would possess. The purpose is not to expose the heel of the system to a mortal

> dart—not, in other words, to open to taxation what is not within the state."

It was thus stated in *Norfolk & Western* v. *North Carolina* (1936) 297 U. S. 682, 80 L. ed. 977, 56 S. Ct. 625:

> "This is not to say that a tax is valid as imposed. A formula not arbitrary on its face or in its general operation may be unworkable or unfair when applied to a particular railway under particular conditions . . . If this is made to appear with an ensuing burden on the taxpayer grossly in excess of the results of a more accurate apportionment, the statute to that extent is an unconstitutional endeavor to tax the income of a business in another jurisdiction."

And finally the statute as indicated in *Norfolk & Western, supra,* must be

> "the outcome of a reasonable endeavor to arrive at a proportion of general validity."

It must not seek to accomplish any other purpose than "to get the true value of the things within" the state. It must not be designed to "open to taxation what is not within the state" or to discriminate against one class of taxpayers in favor of another.

This case is distinguishable from *Ford Motor Co.* v. *Beauchamp,* 308 U. S. 331, 84 L. ed. 304, 60 S. Ct. 273 (1939), rehearing denied 308 U. S. 640, 84 L. ed. 531, 60 S. Ct. 273 (1940), where no contention was made that the allocation factor did not adequately reflect the contribution to total capital stock value of the taxpayer's property and business in its Detroit headquarters, including, no doubt, its considerable investment in subsidiaries. In that case the taxpayer argued that the apportionment formula apportioned to the taxing state a capital stock value far in excess

of the real market value of the tangible property in Texas considered in isolation. This issue is not comparable to the issue presented here.

This case is comparable in all essential respects to *Wallace* v. *Hines, supra.* The apportionment of total value of outstanding stocks and bonds in that case on a mileage factor corresponds to the apportionment of total net worth value in this case on a gross receipts factor. The contribution to total outstanding stock and bond value of the extensive out-of-state terminals of the railroad in that case which the mileage factor failed to measure corresponds to the contribution to total net worth of the out-of-state property and business of appellant's headquarters and commercial domicile which the gross receipts factor in this case fails adequately to measure. And the contribution to total capital stock and bond value of the out-of-state investment portfolio in that case which the mileage factor failed to measure corresponds to appellant's out-of-state investment in its subsidiaries which this gross receipts factor fails adequately to measure. The apportionment reviewed in *Wallace* v. *Hines, supra,* was held to be invalid.

This case is also comparable to *Hans Rees' Sons* v. *North Carolina, supra.* There a single apportionment factor of *property* did not adequately measure the contribution to entire net income of economic activity outside the state. Here the single gross receipts factor does not adequately reflect in fact the contribution to entire net worth of the out-of-state investment in subsidiaries and other headquarters assets. See Altman and Keesling, *Allocation of Income in State Taxation* (C. C. H., 1950, 2nd ed.) 97, 108, 118.

As in *Wallace* v. *Hines* and *Hans Rees' Sons* v. *North Carolina,*—and in contrast to *Ford Motor Co.* v. *Beauchamp,*

—it is respectfully submitted that the uncontradicted evidence offered in the Division of Tax Appeals by Taxpayer is clear and cogent that New Jersey has measured its tax against Taxpayer by extraterritorial values. Its tax base is demonstrably too big in comparison with all other measurement techniques adduced; its apportionment method is incapable of application as a principle to various wholly genuine parts of Taxpayer's net worth; there is nothing conjectural about the accountancy reasons for this result. In short, New Jersey has taxed the exercise of franchises with which it has nothing to do, and would more or less completely exempt from taxation the same franchises if exercised within New Jersey by a comparable corporation with a local commercial domicile. The record demonstrated, not only the fact of extraterritorial tax impact, but the actual dollar extent of it and the reasons why it occurred.

Appellant's factual situation is not unique. Many multistate corporations have wholly owned subsidiaries and make advances to them. Foreign countries and various of the United States may require that business done within their jurisdictions shall be by corporations locally incorporated. Foreign countries and individual states may grant special powers to corporations locally incorporated which create opportunities not available to foreign corporations. Most corporations own bank balances, bonds, and similar assets on which the gross rate of return is nil or materially lower than the gross return such corporations receive from their dealings with customers. These intangibles normally have a tax situs at the corporation's home office, where the corporation is also subject to tax.

Every multistate corporation also has a home office located in a specific state. The corporate franchise to maintain that office involves the use within the state of sub-

stantial amounts of capital and labor which subjects the corporation to taxes in that state on a proportionate part of its total net worth. See *Adams Express Co.* v. *Ohio State Auditor*, 166 U. S. 185, 224-225, 41 L. ed. 965, 979, 17 S. Ct. 604 (1897).

It will gravely restrict the opportunities available to multistate corporate managements if their use of subsidiaries subjects them to state taxation on their extraterritorial values.

The Commerce Clause of the Constitution has been exhaustively construed by this Court in the field of state taxation. So long as it was originally a prohibition against any state taxation burdening interstate commerce, it was the primary consideration in tax cases. Lately the prohibitory effect of the Commerce Clause has been relaxed, so that earlier decisions of this Court construing the Fourteenth Amendment as a restriction on the right of any state to tax values outside that state's territory have received a new importance. Congress is presently analyzing multistate taxation for the purpose of enacting legislation to promote uniformity of such taxation within stated restrictions, and undoubtedly would benefit from a restatement, by this Court in this appeal, of 14th Amendment principles in the light of modern interstate and international business organization.

The questions under the 14th Amendment raised by this record, therefore, are important to most multistate corporate taxpayers, to all state legislatures and tax administrators in states using a gross receipts allocation method, and to Congress. The impact of the 14th Amendment on the power of a state to tax extraterritorial values presents questions of such substantial merit, as to require plenary consideration with briefs on the merits and oral argument for their resolution.

Conclusion.

This Court can advance the science of multistate taxation immeasurably by accepting this appeal as presenting a substantial federal question. There have been very few cases heard recently and in detail by this Court arising under the 14th Amendment and requiring the review of evidence claimed to show the taxation of "extraterritorial value", especially when unencumbered by the Commerce Clause.

The issue is whether a method for apportioning total net worth value within or without the taxing state is valid under the 14th Amendment when it uses a gross receipts formula in which the gross receipts in the numerator and the gross receipts in the denominator, respectively, has no comparable relation to net worth.

Respectfully submitted,

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Dated: July 9, 1962.

Appendix A.

Opinion, Order on Petition for Rehearing and Mandate of Supreme Court of New Jersey.

SUPREME COURT OF NEW JERSEY,

A-47—SEPTEMBER TERM—1961.

HOUSEHOLD FINANCE CORPORATION,
a Delaware Corporation,
Appellant,

v.

DIRECTOR OF THE DIVISION OF
TAXATION,
Respondent.

Argued November 20 and 21, 1961. Decided January 22, 1962.

The opinion of the court was delivered by WEINTRAUB, C. J.

This case involves assessments against Household Finance Corporation (herein "Household") under the New Jersey Financial Business Tax Law (1946), N. J. S. A. 54:10B-1, *et seq.*, for the years 1954 to 1957, inclusive. The Division of Tax Appeals sustained the assessments and we certified Household's appeals before the Appellate Division acted upon them.

The history of the Financial Business Tax Law (1946) appears in *Morris & Essex Investment Co.* v. *Director of Division of Taxation*, 33 N. J. 24 (1960). As there pointed out, the statute was devised against the backdrop of the federal statute, 42 Stat. 1499, 12 U. S. C. §548(1)(b) (1958), which provides that the tax imposed by States upon the shares of national banks "shall not be at a greater rate than

is assessed upon other moneyed capital in the hands of individual citizens of such State coming into competition with the business of national banks." The ultimate criterion under the federal act is whether moneyed capital employed in competition with the business of national banks receives favored tax treatment (33 N. J. at 30). Our taxing statute seeks to achieve equality despite differences in the underlying economics of enterprises which thus compete with national banks.

To that end the statute imposes "an annual excise tax" at the rate of ¾ of 1% upon "net worth" less certain deductions, which tax is "in lieu of any State franchise tax or of any State or local taxation of, upon or measured by personal property entering into the determination of net worth." N. J. S. A. 54:10B-3. With respect to a taxpayer doing business in more than one State, the act provides for an allocation to this State of a portion of its total net worth, "according to the proportion of its gross business in this State to its gross business everywhere during the tax year." N. J. S. A. 54:10B-8.

Household is engaged in the small-loan business. It operates extensively in the United States and also in Canada. In the years in question it maintained between 417 and 445 branch offices in the United States, of which 17 were in New Jersey. It also owned subsidiary corporations which in the United States totaled 24 as of the end of 1953 and numbered 155 by the end of 1956. With one exception, not here significant, the subsidiaries were wholly owned by Household. There were no subsidiaries in New Jersey in 1954; there were two in 1955; seven in 1956, and ten in 1957. Of these, one was active in 1956 and four in 1957. The Canadian business was conducted through subsidiaries. The subsidiaries operating in New Jersey are herein called "New Jersey subsidiaries" although they are foreign corporations, a fact which is of no moment.

Appendix A.

The business conducted directly by Household at its many branch offices was the same as that conducted at the local offices owned by the subsidiaries. So also the operating relationship between Household and the local offices was the same whether they were branches or were individually incorporated. The principal headquarters were in Chicago, and regional offices were maintained in New York, Philadelphia, Detroit, and Los Angeles. Policy decisions were made in Chicago. Supervisory and administrative services, including the training and assignment of local supervisory personnel, were handled there. Services were thus centrally furnished in purchasing, leasehold management, research, advertising, and public relations. Each branch office maintained its own books but reported daily to Chicago where duplicate records were maintained. Headquarters supplied the funds needed by local offices, whether branch or incorporated, to meet the business opportunities as they appeared, and the several offices remitted regularly such funds as headquarters decided to recall.

Household concedes its entire operation was unitary in character.

In its returns for the years in question Household sought in effect to separate its direct operations through branch offices from the operations of the subsidiaries. To that end it first excluded from net worth its equity investment in the subsidiaries. It then applied an allocation fraction in which the numerator was the gross receipts of the New Jersey *branch* offices and the denominator was the gross receipts from all *branches*. Thus Household did not include in the denominator the gross receipts of the subsidiaries or Household's receipts from its subsidiaries.

The Director made a redetermination. He included in net worth the equity investment in subsidiaries. He added to the denominator of the allocation fraction the sums

received by Household from the subsidiaries, *i. e.*, interest, dividends and service fees charged for the sundry services Household furnished the subsidiaries. The Director agreed with Household that with respect to the subsidiaries operating in New Jersey (they filed separate returns), the net worth of Household should be reduced by its investment in them in accordance with N. J. S. A. 54:10B-6(a)(3). Household's receipts from the New Jersey subsidiaries were not included in the numerator of the allocation fraction.

The redetermination thus followed the corporate lines established by Household. Household then complained that the Director, by taking in the shares in subsidiaries at their book value, in effect "consolidated" the enterprise in fixing net worth, and hence should use a "consolidated" approach in fixing the denominator of the allocation fraction by including therein the gross receipts *of* the subsidiaries, rather than only so much as reached Household *from* the subsidiaries by way of interest, dividends and service fees. The sums so paid to Household were less than the gross receipts of the subsidiaries. Hence, if a "consolidated" approach were used, the denominator of the allocation fraction would be enlarged, thereby reducing the portion of total net worth allocable to New Jersey. As we will later develop, Household did not, however, seek a fully consolidated result.

Household also advanced the further claim that its so-called "headquarter assets" were situate in Chicago, and should be deducted from net worth. This contention in fact departed from Household's returns, since therein it had not sought to deduct headquarter assets from net worth.

The Division of Tax Appeals sustained the redetermination. The issues before us are the ones described in the

two preceding paragraphs. We will treat first with the claim that headquarter assets should be excluded from net worth and then consider the attack upon the allocation fraction.

I.

In the years in question the headquarter assets ranged from $21,000,000 to $24,000,000. They included accounts receivable, government securities, office equipment, and deferred charges, but the great bulk consisted of cash on hand, in banks and in transit. For example, at the beginning of 1954, cash amounted to $22,511,984 of total headquarter assets of $24,098,252. The cash items constituted the revolving fund from which Household dispatched moneys to the various local offices to meet the business opportunities there.

As indicated above, Household argues that these assets have their situs in Chicago and that unless they are excluded from net worth, New Jersey would tax extraterritorial values in violation of the due process provision of the Federal Constitution.

The statute does not tax assets beyond the State. Rather, it imposes an excise tax upon the doing of financial business in New Jersey. N. J. S. A. 54:10B-3. That the tax is assessed upon a portion of net worth does not mean that it is an *ad valorem* assessment upon any of the underlying properties. *Werner Machine Co.* v. *Director of Division of Taxation*, 17 N. J. 121 (1954), affirmed, 350 U. S. 492, 100 L. Ed. 634 (1956). Net worth simply sums up the relationship between assets and liabilities and thus expresses the experience of an enterprise. It is not "property" and of course is not an "asset" in a balance sheet. It is merely a concept, without tangible situs in any specific asset.

Appendix A.

In a sense, the excise tax may gather the hue of a property tax, but if so viewed, it is the franchise to do local business that is being valued rather than any specific piece of property devoted to it. In thus appraising the worth of a franchise, it is fitting to refer to "net worth," for the franchise ultimately contributes to that balance-sheet result. And in dealing with a multi-State business, unitary in nature, it is reasonable to assume the franchise to do business in this State contributes to the net worth in the proportion that the business done here bears to the total business of the taxpayer.

Hence in assaying the value of the business privilege in this State, the important thing is the business done here. In this frame of reference, the location of headquarters was of no moment. Headquarter assets were part of an operating whole, and were employed wherever the taxpayer did business. They were directly employed in New Jersey to the extent that cash was sent here as needed, and the tangible property stationary at Chicago was devoted to New Jersey activities with the same immediate effect as if the equipment were within our borders. Indeed, in terms of the small-loan business to which Household's enterprise was devoted and from which its net worth emerged, the headquarter assets were wholly unproductive within the walls of the home office; they generated results only by meaningful employment at the sundry places where the small loans were made.

If we recur to the legislative purpose mentioned above, *i.e.*, to prevent tax preference for competitors of national banks, we find confirmation of the conclusion we have reached. It is the business done in this State which competes with the national banks. The tax imposed upon competitors should take into account the amount and value of that business. The headquarter assets contributed to

the competition in this State as effectively as if that reservoir were here. They accordingly should not be excluded in calculating the net worth of the unitary operation.

In *Household Finance Corp.* v. *State Tax Comm'n*, 212 Md. 80, 128 A. 2d 640 (Ct. App. 1957), this taxpayer advanced without success the same contention we have rejected. There the taxpayer urged the inclusion of headquarter assets in ascertaining the value of its capital stock violated the Federal Constitution. The Maryland court found no substance in the claim.

We think the issue is controlled by *Ford Motor Co.* v. *Beauchamp*, 308 U. S. 331, 336, 84 L. Ed. 304, 306-07 (1939), where the Court said:

> "In a unitary enterprise, property outside the state, when correlated in use with property within the state, necessarily affects the worth of the privilege within the state. Financial power inherent in the possession of assets may be applied, with flexibility, at whatever point within or without the state the managers of the business may determine. For this reason it is held that an entrance fee may be properly measured by capital wherever located. The weight, in determining the value of the intrastate privilege, given the property beyond the state boundaries is but a recognition of the very real effect its existence has upon the value of the privilege granted within the taxing state."

II.

The remaining question concerns the allocation formula —the statutory fraction in which the numerator is the gross receipts in New Jersey and the denominator is the total gross receipts of the business.

Appendix A.

It is settled that an apportionment formula will be sustained unless it is "palpably unreasonable," and the burden is the taxpayer's to prove by "clear and cogent evidence" that it results in the taxation of extraterritorial values. *Railway Express Agency* v. *Virginia*, 358 U. S. 434, 443, 444, 3 L. Ed. 2d 450, 457 (1959).

To sustain its charge, Household offered testimony of other possible bases of apportionment, such as payroll, assets, etc. Its witness conceded all of his suggestions contained some defects. The question is not whether some other technique could be used, but whether the formula the Legislature selected is palpably unfair. An allocation formula based upon gross receipts seems to us to be thoroughly sound when applied to a business such as Household's. Surely the formula does not bespeak an invidious purpose to tax what is not here. And a result of that character is not shown by proof that some basis other than gross receipts would yield a smaller tax. We find no demonstration that a gross-receipts fraction allocated to New Jersey a portion of net worth beyond that in fact attributable to New Jersey business.

The troublesome aspect of this case stems, not from the use of a gross-receipts formula, but rather from the fact that Household operated in part through branch offices and in part through subsidiaries. The Director included in net worth the value of Household's shares in its subsidiaries. This was plainly correct since the shares were an integral part of the total assets which constituted the strength against which Household was able to borrow huge sums at favorable rates, which sums it parceled out among the local offices for small loans by them. Household does not now question the inclusion of the shares or the use of book value in their valuation. Rather it complains of the allocation fraction the Director used. As we have already noted,

the Director, in preparing the allocation fraction, did not include the gross receipts of the subsidiaries, but rather only such sums as Household received from them by way of interest on advances (which was at a lesser rate than the subsidiaries collected on small loans), dividends (as a matter of Household's own policy, the subsidiaries in the United States declared no dividends in the years in question), and service fees which Household received from the subsidiaries.

The Director thus dealt with Household in accordance with its own corporate structure. The redetermination was upon an "unconsolidated" basis. The statute does not authorize a consolidated return. *General Public Loan Corp.* v. *Director of the Division of Taxation*, 13 N. J. 393, 400, 404 (1953). So N. J. S. A. 54:10B-6(a)(3) provides there may be deducted from net worth the value of shares "in corporations taxable under this act" upon the formula there set forth. N. J. S. A. 54:10B-7 and 8 continue the non-consolidated theme. Indeed by chapter 308 of L. 1950 the section last cited was amended to provide with respect to multi-State operations that a wholly owned subsidiary having capital stock with a par or stated value of $5,000 or less be deemed, in effect, a part of the taxpayer's direct business operation. The statement annexed to the bill which became that amendatory act reveals the evident purpose of giving "the benefit of the allocation provision" to taxpayers doing business in other States through such subsidiaries, "a situation comparable to that of a taxpayer doing business directly in other States." Thus the Legislature expressly determined to permit consolidation only with respect to subsidiaries of such limited capitalization.

There is nothing inherently wrong with the statutory plan. The alleged hardship ensued solely from Household's decision to operate in part through subsidiaries. Although

the cases recognize that a formula fair on its face may offend constitutional limitations when in its actual operation it plainly taxes extraterritorial property or activity, *Hans Rees' Sons, Inc.* v. *North Carolina ex rel. Maxwell*, 283 U. S. 123, 75 L. Ed. 879 (1931); *Wallace* v. *Hines*, 253 U. S. 66, 64 L. Ed. 782 (1920), we know of no case in which constitutional infirmity was grounded upon a refusal to disregard corporate lines.

The issue was advanced in *Household Finance Corp.* v. *State Tax Comm'n, supra* (212 Md. 80, 128 A. 2d 640), where a consolidation was found, by a vote of 3 to 2, to be authorized by the statute itself, the majority not reaching the question whether the result was constitutionally required. A similar contention was rejected in *Commonwealth* v. *Ford Motor Co.*, 350 Pa. 236, 245-46, 38 A. 2d 329, 334 (Sup. Ct. 1944).

We are not told why Household employed subsidiaries. A probable motivation was tax advantage somewhere. The question is whether a State must adjust its tax laws to avoid a disadvantage a taxpayer may experience because of its decision to incorporate a part of its operation. As a general proposition, the answer must be that it is for the taxpayer to make its business decisions in the light of tax statutes, rather than the other way around. See *Higgins* v. *Smith*, 308 U. S. 473, 477, 84 L. Ed. 406, 411 (1940); *Vim Securities Corp.* v. *Commissioner*, 130 F. 2d 106, 109 (2 Cir. 1942); *Bonnar-Vawter, Inc.* v. *Johnson*, ... Me. ....., 173 A. 2d 141 (Sup. Jud. Ct. 1961); *Washington Sav-Mor Oil Co.* v. *Tax Comm'n*, ... Wash. 2d ....., 364 P. 2d 440 (Sup. Ct. 1961); Annotation, 64 A. L. R. 2d 769 (1959).

The authorities just cited may not be precisely in point, since they did not involve the problem of apportionment of a tax base of a multi-State business. Nonetheless, corporate lines are real. Moreover, taxation is an intensely practical

thing, and the administrative burden may well be too much if a State must explore the ramifications of corporate structures to determine the justice of recognizing or ignoring corporate entities in each factual complex.

At any rate we need not decide whether a consolidated approach would have to be allowed in a case in which it cogently appeared an unconsolidated basis allocated a portion of net worth palpably beyond what is reasonably attributable to the New Jersey activity. First, the facts do not demonstrate a palpable misapportionment. *Cf. Norfolk & W. Ry.* v. *North Carolina ex rel. Maxwell*, 297 U. S. 682, 80 L. Ed. 977 (1936). Second, Household did not seek consolidated treatment.

What Household sought was a hybrid result under which its corporate lines would be respected as to New Jersey operations and disregarded elsewhere. More specifically, Household wanted the right to file separate returns for the New Jersey subsidiaries while using a consolidated approach with respect to the others. It in fact did file separately for the New Jersey subsidiaries, and upon the redetermination insisted before the Director that their net worth be excluded from total net worth under N. J. S. A. 54:10B-6(a)(3), a proposition with which the Director agreed. So also Household excluded the gross receipts of New Jersey subsidiaries from the allocation fraction.

After oral argument we sought clarification of Household's position in this respect. We were informed:

> "However, the statute (§6) requires that Taxpayer's subsidiaries which are active in New Jersey be separately taxed on their own local franchises. The statute shows a clear legislative intent to draw a distinction between the local subs' own franchise to operate locally, which is separately taxable, and

> the Taxpayer's distinctive franchise to own those subs, which is taxable or not according to where it is held and exercised. Accepting the statutory distinction (as both parties do), the problem is simply to measure the portion of Taxpayer's net worth which represents this value and to determine its taxable situs."

and further:

> "* * * Moreover, if the disregard of corporate lines appears to be only a partial one (that is, the middle ground under which Taxpayer's New Jersey subs are fractioned off individually), this is solely because of the explicit requirements of §6, which requirements, incidentally, both parties accept and which therefore should be accepted by the Court as binding for the purposes of this appeal."

Quite obviously, if the gross receipts of the New Jersey subsidiaries were included in the numerator and denominator of the allocation fraction, the fraction would be enlarged. This is apparent from a simple example, let us say, of adding 5 to the numerator and denominator of the fraction 5/20 which would result in the fraction 10/25. If the fraction, augmented above and below the line by the gross receipts of the New Jersey subsidiaries, were applied to the total net worth, the portion allocable to New Jersey would not necessarily be the same as the total of (1) the net worth of the New Jersey subsidiaries and (2) the portion of Household's remaining net worth allocated to New Jersey by a fraction having the New Jersey branch office receipts as the numerator and "consolidated" gross receipts as the denominator. We do not know the tax-dollar consequences for the

years in question of that dual approach, but it seems clear that, in espousing the split approach we have described (*cf. Household Finance Corp.* v. *State Tax Comm'n*, 217 Md. 327, 142 A. 2d 807 (Ct. App. 1958)), Household seeks an opportunity to control its total tax by the expedient of deciding which New Jersey offices to operate through subsidiaries and which to operate as branches.

The statute permits Household to operate in New Jersey through subsidiaries with separate treatment of them. Household simply seeks to fashion still another choice, whereby it may "consolidate" its out-of-State operations while maintaining the integrity of corporate lines with respect to the New Jersey segment of its total operations. The statute does not permit and surely due process does not require that incongruity.

The judgments are affirmed.

Appendix A.

Order on Petition for Rehearing.

SUPREME COURT OF NEW JERSEY

HOUSEHOLD FINANCE CORP., Appellant, *vs.* DIRECTOR, DIVISION OF TAXATION, Respondent.	Docket No. 3573 On Petition for rehearing.

This matter having been duly presented to the Court, and no justice who voted with the majority having moved a reconsideration, it is Ordered that the petition for rehearing is denied.

Witness, the Honorable Joseph Weintraub, Chief Justice, at Trenton, this 26th day of March 1962.

JOHN H. GILDEA
Clerk

Filed.
Mar. 26, 1962.

JOHN H. GILDEA
Clerk

A True Copy

JOHN H. GILDEA
Clerk.

Appendix A.

Mandate on Affirmance.

SUPREME COURT OF NEW JERSEY.

APPEAL DOCKET NO. 3575.

HOUSEHOLD FINANCE CORPORATION, a Delaware Corporation,
Appellant,
vs.
DIRECTOR OF THE DIVISION OF TAXATION,
Respondent.

Civil Action
On Appeal

This cause having been duly argued before this Court by Mr. Roger C. Ward, counsel for the appellant and Mr. Alan B. Handler, counsel for the respondent, and the Court having considered the same,

It is hereupon ordered and adjudged that the judgments of the said Division of Tax Appeals are affirmed with costs; and it is further ordered that this mandate shall issue ten days hereafter, unless an application for rehearing shall have been granted or is pending, or unless otherwise ordered by this Court, and that the record be remitted to the Division of Tax Appeals to be there proceeded with in accordance with the rules and practice relating to that court, consistent with the opinion of this Court.

WITNESS the Honorable JOSEPH WEINTRAUB, Chief Justice, at Trenton on the 22nd day of January, 1962.

FILED
Jan 22 1962
JOHN H. GILDEA
Clerk

JOHN H. GILDEA,
Clerk of the Supreme Court.

A True Copy

JOHN H. GILDEA
Clerk.

Appendix B.

Opinion and Judgment of Division of Tax Appeals, State of New Jersey.

STATE OF NEW JERSEY

DEPARTMENT OF THE TREASURY

DIVISION OF TAX APPEALS

HOUSEHOLD FINANCE CORPORATION,
A Delaware Corporation,
Petitioner,

vs.

DIRECTOR OF THE DIVISION OF TAXATION,
Respondent.

Opinion

KOPP, C.

This is an appeal by the petitioner, Household Finance Corporation, a Delaware Corporation, authorized to do business in New Jersey, from taxes assessed against it by the respondent, Director of the Division of Taxation, under the Financial Business Tax Act, N. J. S. A. 54:10B-1 *et seq.* for the tax years 1954, 1955, 1956 and 1957. After a pretrial before the Division of Tax Appeals sitting *en banc*, the matter was assigned to me under N. J. S. A. 54:2-41.1 (a) and Rule 16:8-10.100 (1) for hearing and determination and the hearing was held on January 12, 1960. Thereafter, both parties filed briefs and supplemental briefs.

FACTS.

Petitioner is and was engaged in the business of lending money at branch offices within and without New Jersey.

Appendix B.

During the years in question it owned and operated within this State 17 branch loan offices and outside of New Jersey it owned and operated some 417 to 445 branch offices in 27 or 28 states as licensee under state small loan or similar laws. Petitioner's business in New Jersey is a "financial business" within the meaning of Section 2(b) of the New Jersey Financial Business Tax Law, (1946), N. J. S. A. 54:10B-1 *et seq.*, and was subject to the tax imposed by said statute.

In addition to conducting its financial business through branch offices, petitioner also owned, managed and controlled all, or substantially all, of the capital stock of certain subsidiary corporations, none of which were New Jersey corporations. Such subsidiaries were engaged in the business of lending money in the various states of the United States or in Canada, and some subsidiaries operated in New Jersey. On its books and in its New Jersey Financial Business tax returns, petitioner carried and reported its investment in the stock of its subsidiaries at cost.

Petitioner maintains its headquarters office in Chicago, Illinois, with regional headquarters offices during the years in question in New York, Philadelphia, Detroit and Los Angeles. Headquarters furnishes all branch offices, subsidiaries and subsidiary branch offices with similar accounting, advertising, supervisory and other administrative services. Personnel is sometimes interchanged among the branches, subsidiaries and subsidiary branches. Money to lend is forwarded by headquarters to all branches and subsidiaries and all remit any excess of funds to or as directed by headquarters. Each branch office maintains its own books of account but makes daily reports to headquarters where a duplicate set of accounts is maintained.

Petitioner owns no real property. All offices, both headquarters and branch, are rented. The same applies to the

subsidiaries except that one of the Canadian subsidiaries owns the premises in Toronto in which the Canadian principal administrative office is located. The tangible assets of petitioner consist almost entirely of office equipment and its intangibles consist principally of notes receivable from customers and stock in and advances to subsidiaries.

Receipts of petitioner consist of interest collected from customers through its own branch offices and dividends, interest and supervision fees from subsidiaries. All subsidiaries were regularly charged a supervision fee which was determined as a proportion of the general administrative expenses. As to U. S. subsidiaries the apportioning factor was the average of the ratios of number and amount of loans outstanding to total. The formula as to Canadian subsidiaries was slightly different.

Petitioner duly filed its Financial Business Tax Returns for the tax payment years in question, i. e., 1954, 1955, 1956 and 1957 and in each of said returns, it computed what it termed its "New Jersey Taxable Net Worth" as of December 31 of the year preceding the particular tax-payment year as follows:

(a) Its entire net worth per its books was increased by decreasing its bad debt reserve to conform to what it then believed to be the requirement of the Division of Taxation.

(b) It then excluded from its net worth, as so adjusted, that part of it represented by what it termed its "non-financial or holding company business outside of New Jersey". This was done by excluding from its total net worth, that proportion thereof which the value per books of its stock in, and advances to, its subsidiaries bore to petitioner's total assets per books.

Appendix B.

(c) Of the remaining net worth which petitioner termed its "Financial Business Net Worth", the petitioner then allocated that part of such "Financial Business Net Worth" as was represented by its financial business within New Jersey. This was done by allocating to New Jersey that proportion of its total "Financial Business Net Worth" which the petitioner's gross income from its financial business within New Jersey, bore to its total gross income from its financial business both within and without New Jersey. This residue petitioner termed its "New Jersey Taxable Net Worth". In making this allocation petitioner excluded from "financial business gross income", both within and without New Jersey, all interest, dividends and supervision fees received from its subsidiaries.

Petitioner's method of determining "New Jersey Taxable Net Worth" may be illustrated by reviewing such computation for the year 1954, which is as follows:

1.	Entire net worth per books	$102,229,444.00
2.	Adjustments:	
	(a) Add, adjustment of bad debt reserve	11,220,171.00
		$113,449,615.00
	(b) Deduct, non-financial net worth	31,491,196.00
3.	Balance represents "financial business net worth"	$ 81,958,419.00
4.	Line 3 x 5.88148018%* equals "New Jersey Taxable Net Worth"	$ 4,820,368.00

* 5.88148018% being the ratio equivalent to the fraction:
New Jersey Financial Business Gross Income (over)
Financial Business Gross Income within and without N. J.

Appendix B.

On July 29, 1957 the Corporation Tax Bureau notified petitioner of a redetermination of its tax liability for each of the four years 1954 to 1957 both inclusive. By such redetermination the Bureau recomputed petitioner's "New Jersey Taxable Net Worth" as set forth on the tax returns filed for each of said years, in the following manner:

(a) The Bureau first increased petitioner's total net worth (as adjusted by petitioner in said returns), by adding thereto certain amounts representing dividends payable to petitioner's stockholders holding more than 10% of petitioner's total outstanding stock, as required by N. J. S. A. 54:10B-2(c)(1)(5).

(b) The Bureau then decreased such adjusted net worth by increasing petitioner's bad-debt reserve to an amount equal to the moving average loss experience, plus a 1% safety factor.

(These two adjustments (a) and (b) are not in issue.)

(c) To petitioner's total net worth as so adjusted the Bureau then added an amount equal to the excess of the fair value of the petitioner's investment in stock of subsidiaries over the amount reported as the value on the petitioner's returns.

(d) As a further adjustment the Bureau then restored to total net worth the amount excluded by the petitioner as being that portion of its net worth represented by what it termed its "non-financial or holding company business outside of New Jersey". The resulting amount was considered by the Bureau to represent the petitioner's total adjusted net worth.

(e) The Bureau then allocated to New Jersey that proportion of total adjusted net worth which petitioner's gross income from business within New Jersey bore to the sum of petitioner's gross income from both within and without New Jersey. The gross

income so used included interest, dividends and supervision fees received from subsidiaries. The resulting amount was determined by the Bureau to be the petitioner's taxable net worth on which the tax was computed.

The Bureau's method of determining Taxable Net Worth may be illustrated by reviewing such computation for the year 1954, which is as follows:

1. Net worth reported by petitioner (termed financial business net worth)	$ 81,958,419.00
2. Adjustments	
(a) Add, dividends payable to stockholders	294,000.00*
(b) Deduct, increase in reserve for bad debts	(1,749,893.00)*
	$ 80,502,526.00
(c) Add, increase to bring value of subsidiaries to true value	12,738,094.00
(d) Add, amount excluded by petitioner as representing net worth of non-financial business	31,491,196.00
3. Adjusted net worth	$124,731,816.00
4. New Jersey allocation percentage (ratio of total gross income from within N. J. to total gross income from within and without N. J.)	5.6187%
5. Taxable net worth (line 3 x line 4)	$ 7,008,307.00

* These adjustments are not contested by petitioner.

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The redetermination resulted in an assessment of additional taxes for each of the four years in question which together with the interest charged thereon aggregated $55,498.52 which petitioner paid, under protest, on August 12, 1957. Thereafter, petitioner sought and obtained a formal hearing before the Supervisor of the Bureau, who sustained the Bureau's assessments and this appeal followed.

CONTENTIONS OF PETITIONER.

Briefly stated, petitioner's arguments against respondent's redeterminatiion are as follows:

1. Petitioner asserts that in addition to its general small loan business operated through its branches, it also engaged in a holding company business, consisting of beneficially owning, holding, managing and controlling all, or substantially all, of the capital stock of certain subsidiary corporations. It admits that its entire business may be viewed as a unitary one in that its subsidiaries and their financial business are related to the rest of its financial business both by the normal corporate and financial relationship of subsidiary to parent and in an economic operating sense, but it argues that the subsidiaries and petitioner's business with respect to them are located and operated outside New Jersey and that this integral part of the unitary business must be accurately and fully segregated out of the New Jersey tax base.

And further, in this regard, petitioner urges th[illegible] if it be found (and this it does not concede) that this foreign business did cast any indirect value upon the New Jersey franchise, this should be measured by reasonably accurate apportionment and measurement of the New Jersey franchise itself. This respondent has failed to do and, instead,

has incorporated it into the tax base and, therefore, directly taxed this extraterritorial value.

2. Petitioner argues that its total net worth reflected (among other things) the value according to its books of its investment in certain property, both tangible and intangible, which it termed "Headquarters Property". Such property was located at its home office in Chicago, Illinois, and consisted of general corporate cash on hand and in banks; headquarters office equipment, and certain other miscellaneous items. Since said Headquarters Property, although used in the management of petitioner's entire business, was located entirely outside of New Jersey, that proportion of petitioner's net worth which said Headquarters Property bore to petitioner's total assets, was and is outside the territorial limits of, and not taxable by, New Jersey. Therefore, in determining petitioner's New Jersey Taxable Net Worth the aforesaid proportion of net worth should be excluded from petitioner's adjusted net worth, in order to exclude from taxation by New Jersey the portion thereof represented by such non-income producing Headquarters Property located outside New Jersey.

3. Petitioner argues that respondent erred in increasing its net worth as reported by an amount equal to the amount by which the book value of petitioner's stock in its subsidiaries per the subsidiaries' books exceeded the book value, or cost thereof, per the petitioner's books. Such an adjustment, it urges, is equivalent to valuing petitioner's net worth on a consolidated basis.

4. Petitioner argues that respondent was wrong in his method of computing the New Jersey allocation factor in three respects. (a) Inclusion in gross income of dividends,

interest and supervision fees received from subsidiaries was improper since such receipts were no part of petitioner's gross income from its financial business as defined in N. J. S. A. 54:10B-8.

(b) The inclusion of petitioner's receipts from its subsidiaries on an unconsolidated basis was inconsistent with the adjustment and redetermination of petitioner's total net worth on a consolidated inter-company basis. It contends that if it be lawful and proper to redetermine petitioner's total net worth on a consolidated basis, then the statute requires that the petitioner's New Jersey allocation percentage be likewise computed on a consolidated basis.

(c) Petitioner claims that its net worth is separable into three layers. The first represents that portion of net worth invested in headquarters property. The second represents its investment in subsidiaries. The third represents its investment in the business of conducting small loan activities in the several states. This being so, petitioner urges, no one allocation factor should be used to allocate the entire three layer cake but rather each layer should be allocated separately.

5. Petitioner argues that if N. J. S. A. 54:10B-1 *et seq.* must be literally applied, it is unconstitutional because it violates the Constitution of the United States in that the allocation factor as provided by Section 8 thereof, results in exacting a tax on property outside New Jersey without due process and denies a non resident taxpayer equal protection of the law.

6. Petitioner argues that if N. J. S. A. 54:10B-1 *et seq.* is not unconstitutional, the respondent has applied it in an unconstitutional manner and, therefore, in so doing has

violated both the Statute and the Constitution of the United States.

7. Petitioner argues that N. J. S. A. 54:10B-10 permits the respondent to modify the literal meaning of the act and avoid an unconstitutional application thereof.

8. Finally petitioner argues that the inclusion in its net worth of advances it has made to its subsidiaries, who also do business in New Jersey, results in double taxation with respect to the same portion of net worth inasmuch as N. J. S. A. 54:10B-2(c)(1)(5) requires such subsidiaries to include in their net worths amounts owing to their parent. Petitioner complains that Section 6(a) provides only for adjustment in respect to value of stock of subsidiaries and gives no relief in respect to double taxation resulting from inclusion of advances.

CONTENTIONS OF RESPONDENT.

Briefly stated respondent's replies to petitioner's arguments are as follows (Numbered to correspond to petitioner's arguments):

1 & 2. Respondent replies to petitioner's arguments numbered 1 & 2 *supra* that the total net worth of petitioner must be used as the basis of determining New Jersey Taxable Net Worth. There is no provision in the act permitting part of the net worth to be excluded as net worth not employed in a financial business before the allocation for New Jersey Taxable Net Worth is made.

3. Respondent answers petitioner's argument numbered 3 *supra* by stating that N. J. S. A. 54:10B-5 gives the respondent authority to determine the fair value of the

components of net worth. Respondent accepted the values set forth in the books of subsidiaries as representing the fair value of the stocks of such subsidiaries owned by the parent.

4. In response to petitioner's argument numbered 4 (a) (b) and (c) *supra* respondent urges that under N. J. S. A. 54:10B-8 the method of allocating the net worth of a corporation doing a financial business in more than one state is clear and mandatory and that method was employed in making the redeterminations appealed from in this case.

5. In answer to petitioner's argument numbered 5 *supra* respondent simply states that the Division of Tax Appeals has no authority to pass on the constitutionality of an act of the Legislature of the State of New Jersey.

6. To petitioner's argument numbered 6 *supra* respondent replies that N. J. S. A. 54:10B-1 *et seq.* directs the method of allocation of net worth, giving respondent no discretion in making such allocation and that he followed strictly the provisions of said act in making the allocations in this case.

7. Respondent answers petitioner's argument numbered 7 *supra* by urging that N. J. S. A. 54:10B-10 authorizes respondent at his discretion to adjust the allocation of net worth only when it appears to him that the taxpayer maintains places of business outside of New Jersey for the purpose of evading taxes. Since this was not found to exist in this case, respondent had no authority to use any of the alternate methods proposed by petitioner for computing its tax.

8. It does not appear that respondent specifically replied to petitioner's argument numbered 8 *supra*.

Appendix B.

Questions Involved.

The questions required to be answered herein are seven in number and may be concisely stated as follows:

1. Is the Financial Business Tax Law (N. J. S. A. 54: 10B-1 *et seq.*) in violation of the Constitution of the United States?

2. Did respondent in making the redetermination of petitioner's taxes for the years in question exercise any discretion permitted by the statute in such a manner so as to violate the Constitution of the United States?

3. Does N. J. S. A. 54:10B-1 *et seq.* permit a taxpayer to exclude from its net worth investments in subsidiaries or in headquarters property located outside New Jersey?

4. Did respondent under N. J. S. A. 54:10B-1 *et seq.* have authority to increase the net worth, as reported by petitioner, to include the excess of the fair value of its assets over the amount reported in respect thereto?

5. Did respondent comply with the provisions of N. J. S. A. 54:10B 1 *et seq.* in computing petitioner's allocation factor?

6. May the respondent, at his discretion use some alternative method of allocation to determine taxable net worth, and if so, which method should be used?

7. Has petitioner been subjected to double taxation because its advances to its subsidiaries doing business in New Jersey were included once in its total net worth and again in the net worth of the subsidiary, and if so, is it entitled to an adjustment of its taxes?

Appendix B.

After studying the transcript of the record and the briefs submitted by the parties as well as the pertinent statute and cited cases, the Division has reached the following conclusions with respect to the foregoing questions.

The answer to the first question is simple and clear. The Division of Tax Appeals has no jurisdiction to determine the constitutionality of an act of the legislature. Hence, for the purposes of this decision, we are bound to accept N. J. S. A. 54:10B-1 *et seq.* as constitutional. See *Schwartz* v. *Essex County Board of Taxation*, 129 N. J. L. 129 (Sup. Ct. 1942), aff'd. 130 N. J. L. 177 (E. & A. 1943).

With respect to the second question we conclude that it must be answered in the negative. The only area in which respondent exercised his discretion was that permitted by N. J. S. A. 54:10B-5 and this he did in clear accord with the terms thereof. A more extended discussion of this will appear later herein in answer to question 4.

The third question—Does N. J. S. A. 54:10B-1 *et seq.* permit a taxpayer to exclude from its net worth investments in subsidiaries or in headquarters property located outside New Jersey?—must also be answered in the negative. N. J. S. A. 54:10B-3 provides, "There is hereby imposed upon every * * * corporation doing a financial business in this State an annual excise tax * * * upon its net worth, less the deductions hereinafter allowed, * * *." N. J. S. A. 54:10B-6 sets forth the deductions allowed as follows: "For the purpose of determining the measure of the tax hereunder, there may be deducted from net worth: (a) The average aggregate value of the following items held by a taxpayer during a tax year: (1) Shares of stock taxable under the bank stock tax; (2) Shares of stock in domestic insurance companies; (3) Shares of stock in railroad or other public utilities or in corporations taxable under this

act * * *". Obviously the taxpayer's net worth means entire net worth reduced only by the enumerated deductions. None of said enumerated deductions can be construed to include a deduction from total net worth of any portion thereof attributable to investment in subsidiaries or headquarters assets located outside the State of New Jersey, except to the extent of that portion of subsidiaries net worth which may be taxed under this statute.

The fourth question—Did respondent under N. J. S. A. 54:10B-1 *et seq.* have authority to increase the net worth, as reported by petitioner to include the excess of the fair value of its assets over the amount reported in respect thereto?—must be answered in the affirmative.

While N. J. S. A. 54:10B-2 provides that the net worth shall be determined by "the aggregate of the values disclosed by the books of the corporation * * *", N. J. S. A. 54:10B-5 provides:

> "'If in the opinion of the commissioner, the taxpayer's books do not disclose fair valuations the commissioner may require any additional information which may be necessary for a reasonable determination of the net worth which, in his opinion, would reflect the fair value of the assets carried on the books of the taxpayer, in accordance with sound accounting principles, and such determination shall be used as net worth for the purpose of this act."

Pursuant to the clear authority granted respondent by the foregoing provisions he determined that petitioner's books did not reflect the fair value of its stock in subsidiaries and so he adjusted the same to equal the value thereof as disclosed by the books of the respective subsidiary. In so doing respondent accepted such values on subsidiaries' books as being equivalent to the fair value of the respective individual assets owned by the subsidiaries.

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Appendix B.

Where a parent owns one hundred per cent of the stock of a subsidiary, the fair value of all the assets of the subsidiary, less, of course, the liabilities, is an accepted manner of determining the fair value of the asset represented by the ownership of all the subsidiary's stock. Petitioner has not shown that such method is not in accordance with sound accounting principles or that the amount used was actually in excess of fair value.

The fifth question—Did respondent comply with the provisions of N. J. S A. 54:10B-1 *et seq.* in computing petitioner's allocation factor?—must likewise be affirmatively answered.

The provisions of N. J. S. A. 54:10B-8 are applicable to this question and the pertinent parts thereof are as follows:

> "A taxpayer doing business in more than one State • • • shall allocate the value of its net worth (after allowable deductions) within this State, which allocated value shall be the measure of its tax pursuant to this act, according to the proportion of its gross business in this State to its gross business everywhere during the tax year, determined as the sum of:
>
> (a) Fees, commissions or other compensation for financial services rendered within this State;
>
> (b) (Not applicable in this case)
>
> (c) Interest and dividends received on loans, stocks, bonds and other securities managed within this State;
>
> (d) Interest charged to customers, at places of business maintained within this State • • •; and

(e) Any other gross income resulting from the operation of financial business within this State;

divided by the aggregate amount of such items of the taxpayer everywhere."

Now the petitioner complains that the dividends, interest and supervision fees received from its subsidiaries are not "gross business" within the meaning of the above quoted Section 8 and that respondent erred in including such income in determining its allocation factor. It has explained that all its subsidiaries are engaged in the same business as itself, i.e. "small loan business" and were organized for the purpose of engaging in such business where it was necessary or desirable that such business be carried on by a separate corporation. The dividends petitioner has received from its subsidiaries are part of such income.

Petitioner has shown that all its branch offices and subsidiaries forward to the home office their surplus funds, to the extent they exceed their needs to supply the demands of their customers. At the home office these funds are put into a pool, together with funds raised by petitioner from other sources. From this pool monies are supplied to branch offices and subsidiaries who require funds. Interest is charged on the funds supplied to subsidiaries.

With respect to the supervision fees petitioner has clearly established the extent of supervision it exercises through its home office in Chicago. A brief description of that supervisory activity has been set forth earlier herein. Needless to say petitioner through its headquarters office acts as the fully controlling head of the unitary type operation of its vast financial combine. The description of the function of petitioner's headquarters office contained in *Household Finance Corp.* v. *State Tax Commissioner*, 212 Md. 80, 128 Atl. 2d 640 (Ct. of Apps. 1957) is most accurate:

Appendix B.

"• • • Judgments, decisions and policies made and administered out of headquarters tie together and coordinate the activities of its many field offices. It is by the use of sound business judgment at the seat of management, that the life blood of a financial operation like the Household is channeled to those field functions requiring additional capital. Through the operation of its headquarters, and the combined borrowing power, which the complex gives thereto, the most advantages rates of interest may be attained with resultant benefit to all parts of the corporate body. • • • "

Therefore, on the basis of the established facts it must be concluded that amounts received as dividends, interest and supervision fees must be included in "gross business" within the meaning of Section 8. Certainly the dividends received on the stock of subsidiaries are "dividends received on • • • stock • • • ", and interest paid by the subsidiaries on funds advanced by the parent to be in turn loaned to customers of the subsidiaries and the fees paid by the subsidiaries for supervision as herein described are includible in "gross business" from "Fees, commissions or other compensations for financial services rendered • • •" or "Any other gross income resulting from the operation of financial business • • • ". They must all be included in "the aggregate amounts of *such items* of the taxpayer everywhere" (emphasis supplied). That is exactly what respondent did.

The sixth question—May the respondent, at his discretion use some alternative method of allocation to determine taxable net worth, and if so, which method should be used?—arises because of petitioner's contention that N. J. S. A. 54:10B-10 should be repunctuated and so con-

strued as to mean that respondent, in every case where a taxpayer maintains a place of business outside this State, may, in his discretion and in such manner as he may determine, adjust items of net worth, gross business within and without the State and the allocation of net worth as may be necessary for a true and correct determination of the tax. The difficulties with this argument are two in number. First; the section should be read as a whole and with or without commas, the manifest intent was to provide the Director with complete discretion to act whenever it appeared to him that a taxpayer was maintaining a place of business outside the State or doing certain other things for the purpose of evading tax under this act. Only then may he use his discretion to adopt an alternative method of allocation. Plainly the legislature intended that the method of allocation provided in the act was proper and sufficient in all cases except, however, in the case where improper evasion occurred. When that appeared to exist, it then gave the Director broad powers to meet it. Such is not the case here and this section is for that reason inapplicable.

Even if, however, we were to construe it in the fashion urged by petitioner, whether or not such alternative allocation was to be used was a discretionary matter with the Director and we are not sufficiently impressed with petitioner's arguments to find that respondent's failure to exercise that discretion in this case is an abuse of that discretion or resulted in the assessment of an unconstitutional tax.

Finally in answer to the seventh question—Has petitioner been subjected to double taxation because its advances to its subsidiaries doing business in New Jersey were included once in its total net worth and again in the net

worth of the subsidiary?—it must be observed that N. J. S. A. 54:10B-6 provides, in computing net worth, that the taxpayer may exclude from its own net worth a proportion of the value of stock in other corporations subject to tax under this act. There is no provision for a similar adjustment with respect to advances to such corporations. Accordingly, there would be no basis, under the statute, for making such an adjustment and neither the Director nor the Division of Tax Appeals is at liberty to supply such a provision. Any relief in this regard, if needed, must come from the legislature.

In view of the conclusion that such advances may not be adjusted under the statute no relief on this score could be given to petitioner, but it should be pointed out that no competent evidence was offered to prove that the subsidiaries doing business in New Jersey actually had included in their net worth the advances made by petitioner.

Now, in brief summary, the Division finds that the redetermination, as corrected by the minor adjustments pertaining to the exclusion from petitioner's net worth of that part of the value of net worth attributable to subsidiaries doing business in New Jersey which was agreed to by the parties, must be affirmed for the reason that respondent computed the same in accordance with the clear mandate of the Financial Business Tax Law. N. J. S. A. 54:10B-1 *et seq.* Having found that respondent followed the statute as he was required thereby to do, no constitutional question arises which the Division of Tax Appeals has jurisdiction to decide. No consideration, therefore, has been given to the constitutionality of the statute.

Judgment may be submitted in accordance with this opinion.

Appendix B.

Judgment.

STATE OF NEW JERSEY

DEPARTMENT OF THE TREASURY

DIVISION OF TAX APPEALS

HOUSEHOLD FINANCE CORPORATION, A Delaware corporation, Petitioner, *vs.* DIRECTOR OF THE DIVISION OF TAXATION, Respondent.	Judgment

Petitioner having appealed from the determination of the Director of the Division of Taxation redetermining the tax liability of the petitioner under the Financial Business Tax Law for the years 1954 through 1957, and the matter having come on for hearing before Ellis M. Kopp, a member of the Division of Tax Appeals, and good cause therefor appearing,

IT IS ON this 6th day of March 1961 ORDERED AND ADJUDGED that the said determination of the Director of the Division of Taxation, subject to adjustments thereto, to be made upon the filing by the petitioner of claims for deductions for subsidiaries as provided by N. J. S. A. 54:10B-1, *et seq.* and in accordance with the Opinion of the Division of Tax Appeals filed herein, be and the same is hereby affirmed.

DIVISION OF TAX APPEALS

By ELLIS M. KOPP /s/
ELLIS M. KOPP

Appendix C.

New Jersey Financial Business Tax Law (1946), as Amended.

(Quoted Excerpts from N. J. S. A. 54:10B-1, *et seq.*)

"54:10B-2. *Definitions*

"For the purposes of this act, unless the context otherwise requires:

"(a) 'Commissioner' shall mean the director of the division of taxation of the State Department of Taxation and Finance.

"(b) 'Financial business' shall mean all business enterprise which is (1) in substantial competition with the business of national banks and which (2) employs moneyed capital with the object of making profit by its use as money, through discounting and negotiating promissory notes, drafts, bills of exchange and other evidences of debt; buying and selling exchange; making of or dealing in secured or unsecured loans and discounts; dealing in securities and shares of corporate stock by purchasing and selling such securities and stock without recourse, solely upon the order and for the account of customers; or investing and reinvesting in marketable obligations evidencing indebtedness of any person, copartnership, association or corporation in the form of bonds, notes or debentures commonly known as investment securities; or dealing in or underwriting obligations of the United States, any State or any political subdivision thereof, or of a corporate instrumentality of any of them. This shall include, without limitation of the foregoing businesses commonly known as industrial banks, dealers in commercial paper and acceptances, sales finance, personal finance, small loan and mortgage financing businesses, as well as any other enter-

prise employing moneyed capital coming into competition with the business of national banks; *provided*, that the holding of bonds, notes, or other evidences of indebtedness by individual persons not employed or engaged in the banking or investment business and representing merely personal investments not made in competition with the business of national banks, shall not be deemed financial business. Nor shall 'financial business' include national banks, production credit associations organized under the Farm Credit Act of 1933, stock and mutual insurance companies duly authorized to transact business in this State, security brokers or dealers or investment companies or bankers not employing moneyed capital coming into competition with the business of national banks, or any of the following entities organized under the laws of this State: credit unions, savings banks, savings and loan and building and loan associations, pawnbrokers, and State banks and trust companies.

"(c) 'Net worth' shall mean:

"(1) In the case of a corporation—the aggregate of the values disclosed by the books of the corporation for (1) issued and outstanding capital stock, (2) paid-in or capital surplus, (3) earned surplus and undivided profits, (4) surplus reserves which can reasonably be expected to accrue to holders or owners of equitable shares, excluding reasonable valuation reserves and (5) the amount of all indebtedness owing directly or indirectly to holders of ten per centum (10%) or more of the aggregate outstanding shares of the taxpayer's capital stock of all classes, as of the close of a tax year.

* * * * * *

"54:10B-3. *Excise tax imposed*

"There is hereby imposed upon every person, copartnership, association and corporation doing a financial busi-

ness in this State, an annual excise tax, payable in the year one thousand nine hundred and forty-six and in each year thereafter, at the rate of three-fourths of one per centum (¾ of 1%) upon its net worth, less the deductions hereinafter allowed, as of the close of the preceding calendar year, but in no event less than twenty-five dollars ($25.00). Such tax shall also be in lieu of any State franchise tax or of any State or local taxation of, upon or measured by personal property entering into the determination of net worth.

"54:10B-6. *Determining measure of tax; deductions*

"For the purpose of determining the measure of the tax hereunder, there may be deducted from net worth:

"(a) The average aggregate value of the following items held by a taxpayer during the tax year:

"(1) Shares of stock taxable under the bank stock tax;

"(2) Shares of stock in domestic insurance companies;

"(3) Shares of stock in railroads or other public utilities or in corporations taxable under this act; but only in the same proportion that the issuing corporation's total net worth, income or gross receipts, enters into the determination of a tax base under this or any other law of this State;

less such proportion of the total liabilities of the taxpayer (as of the close of the tax year) as the ratio of such average aggregate value to total assets of the taxpayer (as of the close of the tax year); *provided, however,* that, notwithstanding the foregoing, the average aggregate value of any shares of stock described in (1), (2) or (3) held by a taxpayer for more than five years prior to the tax year may be fully deducted from net worth; *and provided further,* that no deduction shall be made or permitted for any shares of

stock described in (1), (2) or (3) above where any indebtedness has been incurred with the intent or for the purpose of acquiring, holding or controlling such stock.

"(b) There may also be deducted from net worth the assessed value of real estate taxable in this State; but such deduction shall not exceed the amount of the taxpayer's equity in such real estate which is included in net worth.

"54:10B-7. *Subsidiary subject to the tax; amount*

"For the purpose of this section, a subsidiary shall be deemed to be any corporation subject to the corporation business tax act in which a taxpayer is the beneficial owner of at least eighty per centum (80%) of the total combined voting power of all classes of stock entitled to vote and of at least eighty per centum (80%) of the total number of shares of all other classes of stock except nonvoting stock which is limited and preferred as to dividends. In determining the measure of the tax imposed by this act, a taxpayer may deduct from its net worth such proportion, not exceeding fifty per centum (50%) of the average value during the tax year of its holdings of capital stock of a subsidiary, less net liabilities (if any) to the subsidiary, as the ratio of the subsidiary's taxable net worth in the tax year (under the corporation business tax act) to its entire net worth.

"54:10B-8. *Corporation doing business in more than one state; allocating value of net worth*

"A taxpayer doing business in more than one State directly or through a wholly-owned subsidiary having capital stock with a par value or stated value of five thousand dollars ($5,000.00) or less shall allocate the value of its net worth (after allowable deductions) within this State, which

allocated value shall be the measure of its tax pursuant to this act, according to the proportion of its gross business in this State to its gross business everywhere during the tax year, determined as the sum of:

"(a) Fees, commissions or other compensation for financial services rendered within this State;

"(b) Gross profits from trading in stocks, bonds, or other securities managed within this State;

"(c) Interest and dividends received on loans, stocks, bonds and other securities managed within this State;

"(d) Interest charged to customers, at places of business maintained within this State, for carrying debit balances of margin accounts, without deduction of any costs incurred in carrying such accounts; and

"(e) Any other gross income resulting from the operation of financial business within this State;

divided by the aggregate amount of such items of the taxpayer everywhere.

* * * * * *

"54:10B-10. *Evading tax; power of commissioner to determine tax*

"Whenever it shall appear to the commissioner that any taxpayer maintains a place of business outside this State, or that any agreement, understanding or arrangement exists between a taxpayer and any corporation, person or firm, for the purpose of evading tax under this act, or whereby the activity, business, receipts or net worth of the taxpayer is distorted for such purpose, the commissioner

may in his discretion and in such manner as he may determine, adjust items of net worth, gross business within and without the State and the allocation of net worth, or make such other adjustments in any tax report or tax return as may be necessary for a true and correct determination of the tax pursuant to this act. The commissioner may require any person or corporation to submit information under oath, or to permit examination of its books, papers and documents, as may be necessary to enable him to determine the existence, nature or extent of an agreement, understanding or arrangement to which this section relates, whether or not such person or corporation is subject to the tax imposed by this act.

Appendix D.

Excerpts from Appellant's Main Brief Filed in Supreme Court of New Jersey.

SUPERIOR COURT OF NEW JERSEY

APPELLATE DIVISION.

DOCKET NO. A-532-60.

HOUSEHOLD FINANCE CORPORATION, a Delaware Corporation, Appellant, *vs.* DIRECTOR OF THE DIVISION OF TAXATION, Respondent.	Civil Action On Appeal from Judgment of Division of Tax Appeals, State Department of Taxation and Finance. Sat Below: Kopp, Member.

• • • • • •

STATEMENT OF QUESTIONS INVOLVED.

1. Did the tax base of purported local net worth upon which appellant's financial business tax liability was computed include extraterritorial values not within New Jersey's jurisdiction to tax?

2. Was the tax base inaccurately and unfairly computed so as to be excessive?

3. Did the financial business tax act require such result, or could it be interpreted to reach a fair and constitutional result?

4. Did the act as applied to appellant deprive appellant of due process of law and equal protection of the laws?

• • • • • •

Appendix D.

CONCLUSION.

If New Jersey has conferred any opportunity, benefits, sanction or protection upon the values represented by taxpayer's headquarters or subsidiary investment as such, the record certainly does not show it and the Attorney General made not even a pretense of proving it. At the risk of tedium, it must be repeated that the record shows and the Director concedes the exact opposite: These values are foreign to New Jersey, they are extraterritorial, the assets are without exception located outside New Jersey, New Jersey has not created or protected the right of a Delaware corporation to own and manage in Illinois (chiefly) headquarters assets and share capital of corporations doing a local business in Maryland, Maine, etc. Nevertheless, New Jersey has taxed these extraterritorial values. Direct proof of this fact is reviewed at length in Point I. New Jersey's tax base is much bigger than it would be under the application of any other sound allocation principle; its allocation method is theoretically unsound; and its seizure of extraterritorial values at the direct expense of the other states is proven empirically, theoretically, algebraically, and by direct uncontroverted testimony.

This harsh, illogical and burdensome result is not required by the taxing statute. There is ample room to interpret the statute fairly, or to mold its literal terms. Point II.

If there were not room to interpret or mold the statute, then it would have to be held to be an unconstitutional deprivation of due process and equal protection of the laws, Point III.

Taxpayer urges that the Court set aside the Director's redeterminations, as affirmed by the Division of Tax Appeals, of its Financial Business Tax Liability for the

tax years 1954, 1955, 1956 and 1957 as violative of the spirit and true construction of the Financial Business Tax Act and contrary to constitutional principles of due process and equal protection of the laws; and that it remand the case in order to reassess Taxpayer's true and just liability for those years by recomputing the tax on the basis of a proper method of allocation.

Respectfully submitted,

PETERS, HARDIN & WARD,
Attorneys for Appellant.

ROGER C. WARD,
FLOYD E. BARTON,
of the Illinois Bar
of Counsel

Appendix E.

Excerpts from Appellant's Petition of Appeal Filed in Division of Tax Appeals, State of New Jersey.

DEPARTMENT OF THE TREASURY

DIVISION OF TAX APPEALS

HOUSEHOLD FINANCE CORPORATION, a Delaware corporation, Petitioner, vs. DIRECTOR OF THE DIVISION OF TAXATION, Respondent.	On Appeal from Redetermination and Assessment of Financial Business Tax Liability for 1954, 1955, 1956 and 1957

Petitioner Household Finance Corporation (hereinafter called the "Taxpayer") appeals to the Division of Tax Appeals from the redetermination of its tax liability under the Financial Business Tax Law (1946), N. J. S. A. 54:10B-1 et seq., made by respondent Director of the Division of Taxation, Department of the Treasury, State of New Jersey, (hereinafter called the "Director"), for the years 1954, 1955, 1956 and 1957; and respectfully shows that: • • •

22. Therefore, Taxpayer petitions for a judgment with respect to Taxpayer's tax liability for the tax-payment years 1954, 1955, 1956 and 1957 under the New Jersey Financial Business Tax Law (1946), [N. J. S. A. 54:10B-1 *et seq.*], as follows:—

A. Sustaining Taxpayer's appeal from those adjustments and redeterminations by the Bureau and by said Director of the Division of Taxation, which Taxpayer has protested and hereby protests as set forth above;

B. Setting aside those adjustments and redeterminations which the Bureau and the Director made, and which Taxpayer has protested and hereby protests, as set forth above;

C. Adjudging and declaring that Taxpayer is entitled to refunds aggregating not less than the $55,498.52 total amount of additional taxes and interest thereon, which Taxpayer paid with respect to said 4 years, as set forth above; and that Taxpayer is also entitled to refunds of such additional amounts of taxes and interest paid by it, as shall be determined and adjudged to have been paid by it in excess of the lawful and proper amounts of Taxpayer's tax liability for said 4 years, under the Statute as correctly and lawfully construed and applied in accordance with the Statute's provisions and the requirements of Section 1 of the Fourteenth Amendment of the Constitution of the United States of America;

D. Adjudging and declaring that, with respect to this Taxpayer and the 4 tax-payment years in question, the Statute, and the adjustments and redeterminations with respect to Taxpayer's tax liability thereunder, which the Bureau and the Director made purportedly under and in accordance with the Statute, are unlawful and unconstitutional, in that the same deprived and deprive Taxpayer of its property without due process of law, and deprived and deprive Taxpayer of the equal protection of the laws, all contrary to Section 1 of the Fourteenth Amendment of the Constitution of the United States of America, because:

(i) A New Jersey financial business tax was imposed upon Taxpayer in respect to values representing property of Taxpayer located outside the territroial limits and taxing jurisdiction of New Jersey; and also

(ii) Such taxes were imposed upon Taxpayer with respect to values wholly unrelated to the true value of Taxpayer's New Jersey financial-business enterprise and franchise; and

E. Granting Taxpayer such other and further relief as may be lawful and proper.

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